

## **EXHIBIT E**

**Stockton USD Audit Report SL 2005 BE 079 12102005**



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December 8, 2005

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KPMG LLP is pleased to submit this performance audit relative to Stockton Unified School District, Beneficiary No. 144339 ("Beneficiary"), for Funding Year (FY) 2002, in accordance with our contract with Universal Service Administrative Company (USAC). USAC engaged us to perform a series of performance audits for FYs 2002 and 2003 to meet the objectives identified in the Objectives and Scope section of this report.

We conducted our audit from January 10, 2005 through December 8, 2005, in accordance with *Government Auditing Standards (2003 Revision)* issued by the Comptroller General of the United States. The purpose of this report is to communicate the results of our efforts. As such, we have captured in the Conclusion; Audit Findings; Other Matters; and Beneficiary and SLD Responses section of this report a detailed discussion of the audit findings and other matters identified during this performance audit, along with responses to our audit findings and other matters from the USAC Schools and Libraries Division and the Beneficiary, with which we shared the results of our audit.

Since December 8, 2005, we have not performed any additional audit procedures with respect to this report and have no obligation to update this report or to revise the information contained therein to reflect events occurring subsequent to December 8, 2005.

KPMG LLP

## **Executive Summary**

We were engaged by Universal Service Administrative Company (“USAC”) to conduct performance audits for Funding Years (“FY”) 2002 and 2003. The objectives of our audits were: (1) to provide an independent assessment of selected beneficiaries’ compliance with the regulations governing the *Schools and Libraries Universal Service Support Mechanism* (“SLSM” or “E-Rate”), set forth in 47 C.F.R. Part 54, and certain USAC implementing procedures which were established consistent with 47 C.F.R. Part 54 and other existing laws or regulations (collectively, “the Rules”); (2) to identify selected beneficiaries’ noncompliance, if any, with certain other USAC implementing procedures related to the SLSM; (3) to identify other beneficiary-specific or SLSM-related conditions that we believe warrant the selected beneficiaries’ or USAC’s attention in an effort to provide greater E-Rate program effectiveness or consistency among beneficiaries; and (4) to identify improper payments made from the Universal Service Fund related to the selected beneficiaries for the years under audit.

### **Scope of Audit**

This report relates to the performance audit conducted relative to Stockton Unified School District, Beneficiary No. 144339 (“Beneficiary”), for FY 2002. The Beneficiary is located in Stockton, California. This performance audit was conducted in accordance with *Government Auditing Standards (2003 Revision)*.

We collaborated with USAC and the Federal Communications Commission Office of Inspector General to develop our basic workplan, and included other procedures when determined necessary to meet the engagement objectives. The scope of this engagement included, but was not limited to, reviewing the Beneficiary’s processes for program application, service provider selection and contracting, and program cost reimbursement.

For FY 2002, amounts totaling \$1,955,840 were disbursed by SLSM on behalf of the Beneficiary under 83 Funding Request Numbers (“FRN”). Those FRNs included amounts for telecommunication services, Internet access and internal connections.

### **Summary of Testwork**

We performed audit procedures on a Beneficiary-wide level related to the application process for participation in the E-Rate program. Those procedures included reading the Beneficiary's audited financial statements, other financial information associated with the E-Rate Program (i.e., other audit reports, budget data, etc.) and technology plan for FY 2002 and evaluating the Beneficiary's calculations of E-Rate discount percentages for which it applied. Our audit was conducted from January 10, 2005 through December 8, 2005.

We selected 11 FRNs, representing 42% of the total amounts disbursed by SLSM for the Beneficiary for FY 2002, and performed audit procedures related to the Beneficiary's service provider selection and contracting and program cost reimbursement processes. To test the Beneficiary's reimbursement process, we selected 21 reimbursement forms from the selected FRNs, which represented 100% of the total disbursed amount under those FRNs. Further, we performed site visits at 16 of the Beneficiary's 46 schools. We determined that the selected schools currently had Internet access and telephone service, which were services funded for FY 2002 under selected Beneficiary-wide FRNs.

### **Summary of Results**

Based on the procedures performed and for the transactions tested, we conclude that the Beneficiary was generally compliant with the Rules identified above for FY 2002, and we identified improper payments of \$21,558. In addition, the result of our audit procedures disclosed two audit findings and two beneficiary-specific other matters, which are reported herein.



## Background

Universal Service Administrative Company (“USAC”) is an independent not-for-profit corporation that operates under the direction of the Federal Communications Commission (“FCC”) pursuant to 47 C.F.R. Part 54. The purpose of USAC is to administer the Universal Service Fund (“USF”), which was created by The Telecommunications Act of 1996 to ensure that consumers in all regions of the United States have access to quality telecommunications and information services at affordable rates. The USF is comprised of four support mechanisms to ensure that the USF objectives are met. USAC has engaged KPMG to perform a series of performance audits for Funding Years (“FY”) 2002 and 2003, including the performance audit to which this report relates.

The USAC Schools and Libraries Division (“SLD”) administers the *Schools and Libraries Universal Service Support Mechanism* (“SLSM”), which makes advanced telecommunications affordable for the nation’s schools and libraries. Also known as “E-Rate”, this mechanism provides discounts on the cost of telecommunication services, Internet access and internal connections, with the highest discounts going to entities serving the most disadvantaged sections of the population. In both Funding Years (“FY”) 2002 and 2003, over 100,000 schools and libraries were funded by the USF.

Stockton Unified School District, Beneficiary No. 144339 (“Beneficiary” or “SUSD”), the subject of this audit, is comprised of 46 schools, and serves approximately 38,000 students. The Beneficiary is located in Stockton, California. For FY 2002, SLD received requests for \$2,915,534 for telecommunication services, Internet access and internal connections from the Beneficiary, and committed and disbursed \$2,387,878 and \$1,955,840 respectively, as summarized in Table 1 below:

**TABLE 1: FY 2002 Dollars Requested, Committed and Disbursed**

Service Category	Requested			Committed			Disbursed		
	# FRNs	Dollars	%	# FRNs	Dollars	%	# FRNs	Dollars	%
Telecommunications	4	\$ 615,396	21.1%	4	\$ 579,197	24.3%	4	\$ 170,956	8.7%
Internet Access	1	33,548	1.2%	1	31,574	1.3%	1	25,993	1.3%
Internal Connections	78	2,266,590	77.7%	78	1,777,107	74.4%	78	1,758,891	90.0%
<b>Totals</b>	<b>83</b>	<b>\$ 2,915,534</b>	<b>100.0%</b>	<b>83</b>	<b>\$ 2,387,878</b>	<b>100.0%</b>	<b>83</b>	<b>\$ 1,955,840</b>	<b>100.0%</b>

## Objectives and Scope

The performance audit was conducted in accordance with *Government Auditing Standards (2003 Revision)*.

The workplan was developed in coordination with USAC and the Federal Communications Commission Office of Inspector General (“FCC OIG”). The objectives of the performance audit were:

- (1) to provide an independent assessment of selected beneficiaries’ compliance with the regulations governing the *Schools and Libraries Universal Service Support Mechanism* (“SLSM” or “E-Rate”), set forth in 47 C.F.R. Part 54, and certain USAC implementing procedures which were established consistent with 47 C.F.R. Part 54 and other existing laws or regulations (collectively, “the Rules”);
- (2) to identify selected beneficiaries’ noncompliance, if any, with certain other USAC implementing procedures related to the SLSM;
- (3) to identify other beneficiary-specific or SLSM-related conditions that we believe warrant the selected beneficiaries’ or USAC’s attention in an effort to provide greater E-Rate program effectiveness or consistency among beneficiaries; and
- (4) to identify improper payments made from the Universal Service Fund related to the selected beneficiaries for the years under audit.

For purposes of this report, the following definitions are provided:

<b>Audit finding</b>	a condition that, in our judgment, evidences non-compliance with the Rules
<b>Other matter</b>	a condition that, in our judgment, evidences non-compliance with USAC implementing procedures not considered in the definition of the Rules or is a condition we believe warrants the Beneficiary’s or USAC’s attention, in an effort to provide greater E-Rate program effectiveness or consistency among beneficiaries
<b>Improper payment</b>	a reimbursement made that, in our judgment, was not in accordance with the Rules.



Following is the timeline and phases for this performance audit:

- |   |                       |                               |
|---|-----------------------|-------------------------------|
| 1 | Planning              | January 10 – 14, 2005         |
| 2 | Fieldwork             | January 18 – February 1, 2005 |
|   | • Entrance Conference | January 18, 2005              |
|   | • Exit Conference     | February 1, 2005              |
| 3 | Wrap-Up / Reporting   | February 2 – December 8, 2005 |

Throughout the fieldwork phase, status updates were provided to the Beneficiary, allowing timely discussions and follow-up on potential audit findings and other matters. Upon completion of the fieldwork, an exit conference was held with the Beneficiary to discuss the results of the audit and the Beneficiary response process. Beneficiary responses, or summaries thereof, are included in the “Conclusion; Audit Findings; Other Matters; and Beneficiary, and SLD Responses” section of this report. The full text of any summarized Beneficiary responses is included in Appendix 2.

We performed the audit procedures described in this report primarily at the Beneficiary’s location and by using information provided to us by USAC and the Beneficiary in advance of our visit to the Beneficiary. As part of the scope of our performance audit, we obtained an understanding of the specific internal controls relevant to the E-Rate program. Because of inherent limitations, a study and evaluation made for the limited purpose of the performance audit would not necessarily disclose all material weaknesses in the internal control structure. Further, this performance audit was not designed to, and does not include a conclusion or opinion on the Beneficiary’s internal control processes.

The performance audit procedures were classified in the following categories: General Procedures; Application Process; Service Provider Selection and Contracting Process; and Reimbursement Process. Following is a summary of the audit procedures performed:

### **General Procedures**

General procedures are those audit procedures that address matters that are not related to any of the identified processes, or those that may have related to all of the identified processes.

*FRN Selection for Testing*

We judgmentally selected 11 Funding Request Numbers (“FRN”) related to the Beneficiary for FY 2002. An FRN is the tracking number assigned by SLD to an E-Rate application for funding. The number of FRNs selected was determined based on the time planned to conduct the performance audit, while attempting to achieve the following two objectives: (1) select at least one FRN from each service category for which disbursement was made from USF funds; and (2) select enough FRNs to achieve at least 25% coverage of total dollars disbursed, with a bias toward FRNs related to internal connections, the service category for which we have evaluated the risk of non-compliance to be the highest. Table 2 below includes a summary of the amounts disbursed by SLSM related to the Beneficiary for FY 2002 in total and under the selected FRNs:

**TABLE 2: FY 2002 Disbursed Dollars in Total and Selected for Testing**

Service Category	Total Disbursed			% of Total Disbursed		
	# FRNs	Dollars		Dollars by Category	# FRNs	% of Total Disbursed Dollars Selected
Telecommunications	4	\$ 170,956		8.7%	1	\$ 134,325 78.6%
Internet Access	1	25,993		1.3%	1	25,993 100.0%
Internal Connections	78	1,758,891		90.0%	9	668,899 38.0%
<b>Totals</b>	<b>83</b>	<b>\$ 1,955,840</b>		<b>100.0%</b>	<b>11</b>	<b>\$ 829,217 42.4%</b>

*Review of Other Audit Reports*

We read the Beneficiary’s Office of Management and Budget (“OMB”) Circular A-133 audit reports for the fiscal years including FY 2002 to identify any findings that may have impacted the Beneficiary’s compliance with the Rules and to determine if the Beneficiary had taken corrective action relative to such findings. No such matters were identified in the Beneficiary’s OMB Circular A-133 audit report for the fiscal year ended June 30, 2003.

We also inquired of USAC and FCC OIG as to whether any other audits or investigations of the Beneficiary, relative to the E-Rate program, had been, or were being, conducted by their respective audit staffs. No such audits or investigations were identified.



## **Application Process**

### *Introduction*

To participate in the E-Rate program, a potential beneficiary must meet certain eligibility requirements. For purposes of this audit, we considered the Beneficiary's financial position, compliance with the Rules related to the Beneficiary's technology plan, and the calculation of the Beneficiary's discount percentage upon application to USAC.

### *Summary of Audit Procedures*

We made inquiries of Beneficiary personnel and examined the Beneficiary's audited financial statements, for the fiscal years relevant to FY 2002, to determine if the Beneficiary had endowments exceeding \$50 million, which would have rendered it ineligible for discounts under the E-Rate program.

We obtained and read the Beneficiary's Technology Plan for FY 2002 and determined whether it was properly and timely approved and included the core elements of successful school and library technology initiatives as identified by USAC.

We examined documentation supporting the Beneficiary's E-Rate discount percentage calculation. To validate the accuracy of the discount percentage, we recalculated the discount percentage in accordance with the eligibility rules for the E-Rate program.

We determined, by reference to the Beneficiary's fiscal year budgets, or other proof of funding, whether the Beneficiary had all of the necessary funding budgeted/available and approved to pay for its non-discounted portion for the requested products and services for FY 2002.

We examined documentation provided by the Beneficiary to determine whether a staff training program, designed to instruct teachers how to incorporate those goods and services into educational instruction, was in place at the time of application for E-Rate funding.

We determined through inquiry of Beneficiary personnel and observation during our site visits (see "Reimbursement Process – Summary of Audit Procedures" below) whether the Beneficiary had the appropriate hardware and software infrastructure to utilize the goods and services for which E-Rate funding was requested.

By examination of E-Rate related documents provided by both USAC and the Beneficiary, we determined whether the Beneficiary indicated compliance with certain requirements of the Children's Internet Protection Act ("CIPA") for FY 2002. Further, we gained an understanding of the Beneficiary's Internet Safety Policy, and the process by which the Beneficiary communicates and administers that policy. During site visits to a selection of the Beneficiary's schools (see "Reimbursement Process" below), we tested certain computers to validate the existence of the Beneficiary's technology protection measure (i.e., filter).

#### *Summary of Audit Findings and Other Matters*

When performing the application process audit procedures, we identified one audit finding related to the Beneficiary not meeting the requirement to have an approved technology budget prior to filing an FCC Form 470, which is reported as Audit Finding No. 144339-F-2002-01 herein.

### **Service Provider Selection and Contracting Process**

#### *Introduction*

The service provider selection and contracting process includes the procurement process and competitive bidding process, when applicable, by which the Beneficiary selected its E-Rate service providers and established its related contracts for eligible goods and/or services. The audit procedures addressed the Beneficiary's procurement process and the eligibility of goods and services procured using E-Rate funds.

#### *Summary of Audit Procedures*

From the 11 selected FRNs, we selected 100% of the related reimbursement forms for use in performing the audit procedures related to the service provider selection and contracting and reimbursement processes. See Appendix 1 for identification of the selected FRNs and reimbursement forms.

We obtained an understanding of the Beneficiary's service provider selection and contracting process, including the related competitive bidding activities, through both discussions with Beneficiary personnel and review of documentation provided by the Beneficiary. We used this information to determine if the design of that process was consistent with the Rules. For the service providers associated with the selected FRNs, we determined whether the Beneficiary followed its service provider selection process procedures, including those for competitive bidding (as applicable), and properly



completed and utilized FCC Forms 470 (Services Requested and Certification Form) and 471 (Services Ordered and Certification Form). We also inquired as to what, if any, assistance the Beneficiary received relative to completion of the FCC Forms and selection of the winning bidders. Further, we determined whether the selected service providers had properly completed FCC Form 473 (Service Provider Annual Certification) for FY 2002.

For each product or service acquired under the selected FRNs, we obtained the service provider bills and related contracts, when applicable. The products and/or services identified on such bills and contracts were compared to the FY 2002 Eligible Services List (“ESL”) published by SLD to determine if those products and/or services were appropriate for E-Rate discount under the Rules. The selected products and/or services identified on the service provider bills and contracts, for which discounts were sought, were also compared to the Beneficiary’s FCC Form 470 to determine consistency of products and/or services described therein.

#### *Summary of Audit Findings and Other Matters*

We identified no audit findings or other matters in performance of the service provider selection and contracting process audit procedures to be reported herein.

### **Reimbursement Process**

#### *Introduction*

The reimbursement process encompasses the Beneficiary’s procedures for processing and paying invoices for allowable program disbursements, the Beneficiary and service providers’ requests for reimbursement from SLSM, and the receipt of reimbursed discounted amounts by the Beneficiary from the service providers, in cases where the Beneficiary had paid such amounts to the service providers prior to disbursement by SLSM. The audit procedures for this process addressed each of the foregoing and included site visits to selected schools to determine if the goods and/or services, for which disbursement was made by SLSM, were in place and operational at the time of our visit.

#### *Summary of Audit Procedures*

We obtained an understanding of the Beneficiary’s cash disbursement process, including invoice review and approval requirements, from discussion with, and documentation provided by, Beneficiary personnel to determine if the design of that process included

safeguards to prevent violations of the Rules. For the selected reimbursement forms (identified in Appendix 1), we determined whether the related service provider bills (either in their entirety or for the beneficiary portion only) were paid in accordance with the Beneficiary's cash disbursement process and that the costs for the products and/or services appeared reasonable. If the service provider bills included any substitute products or services, we compared those items to the FY 2002 ESL and to the substitution authorization issued by SLD.

We obtained the selected reimbursement forms prepared by the Beneficiary (FCC Form 472 – Billed Entity Applicant Reimbursement ("BEAR")) or by the service providers (FCC Form 474 – Service Provider Invoice ("SPI")). The discount percentage claimed on those reimbursement forms was compared to that approved by USAC in the Funding Commitment Decision Letter issued to the Beneficiary and verified whether it was applied appropriately. For service provider bills related to the selected reimbursement forms that included products, we compared the information on the service provider bills (including make, model and serial number, where applicable) to the Beneficiary's asset/inventory records to verify inclusion of these items in the Beneficiary's property records.

For selected reimbursements for which SPI forms were submitted by the service providers, we compared the related bills to the SPI forms to determine whether the service provider sought reimbursement for the appropriate amount from SLSM and whether total billed costs (to SLSM and to the Beneficiary) were less than or equal to the total cost of the eligible products and/or services authorized under the FRN.

For selected reimbursements for which the Beneficiary submitted BEAR forms, we compared the related bills to the BEAR forms to determine whether the Beneficiary sought reimbursement for the appropriate amount from USAC and whether the BEAR form was dated subsequent to the date that the service provider bill was paid by the Beneficiary. We also determined whether the service provider paid the Beneficiary in a timely manner after USAC paid the service provider for the selected BEAR form reimbursements, and we examined evidence of deposit of proceeds by the Beneficiary related to those reimbursements.

We also determined whether the Beneficiary requested reimbursement for less than the amounts committed by USAC under the selected FRNs. If so, and the amount of unused commitment exceeded \$1,000, we determined whether an FCC Form 500 was completed and filed with USAC.



We initially selected the Beneficiary's schools identified in Table 3 below for site visits. The number of schools selected for site visits was determined based on the budgeted time to conduct the site visit component of the performance audit, while attempting to achieve the following two objectives: (1) select at least 5 of the Beneficiary's schools which received services funded by the USF in FY 2002 under the selected FRNs and (2) include schools in our selection which received relatively higher amounts of E-Rate funding and those which received internal connections funding under the selected FRNs, such bias toward internal connections because we have evaluated the risk of non-compliance for internal connections to be the highest of the service categories.

**Table 3: Initial Site Visit Selection**

Entity Number	School
230167	Delores Huerta Elementary
110278	El Dorado Elementary
110286	Fillmore Elementary
110284	Grunsky Elementary
110329	Stagg High School
110328	Walton Special School

For each site visit, personnel with responsibility for overseeing and/or implementing the technology plan were interviewed. The purpose of the interviews were: (1) to determine that the E-Rate funded products and/or services included in the selected FRNs had been received at the school; and (2) to gain an understanding of the use being made of those products and/or services and how the purchased equipment, if any, is safeguarded. We then determined by observing specific items whether the E-Rate funded products and/or services included in the selected FRNs were installed and operational. For site visits to facilities that were administrative buildings, we determined whether the E-Rate funded products and/or services were essential to the transport of information to instructional buildings.

During our site visit to Grunsky Elementary School, we noted eight equipment items that were purchased with E-Rate funds but not found onsite. To better understand the full extent of this issue, we selected an additional 10 schools and revisited the Walton Special School as well as the Beneficiary's storage facility to conduct targeted site visits to focus specifically on the location of E-Rate funded equipment. For these site visits, we did not perform each of the procedures identified above, but instead focused on confirming the existence of E-Rate funded equipment. These schools are identified in Table 4 below.

**Table 4: Expanded Site Visit Selection**

Please note that McKinley is NOT on either list of sites visited.

Entity Number	School
110285	Fremont Middle School
110282	Harrison Elementary School
110272	Hoover Elementary School
110288	King Elementary School
110297	Marshall Middle School
110290	Roosevelt Elementary School
110301	Van Buren Elementary School
110264	Victory Elementary School
110328	Walton Special School*
110265	Washington Elementary School
110273	Webster Middle School

\* Walton Special School was revisited during the expanded set of Beneficiary site visits to verify if any missing equipment was installed at that eligible site.

#### *Summary of Audit Findings and Other Matters*

When performing the reimbursement process audit procedures, we identified one audit finding related to missing and uninstalled E-Rate equipment items, which is reported as Audit Finding No. 144339-F-2002-02 herein. In addition, we identified two beneficiary-specific other matters related to the Beneficiary not completing an FCC Form 500 in a timely manner and inadequate tracking of E-Rate equipment, which are reported as Other Matter Nos. 144339-M-2002-01 and -02 herein.

#### **Conclusion; Audit Findings; Other Matters; and Beneficiary and SLD Responses**

In reaching our conclusion on compliance related to the audit procedures performed and the transactions tested during the performance audit, we considered and based that conclusion on the number of audit findings and the monetary effect of such audit findings.



### ***Conclusion***

Based on the audit procedures performed and for the transactions tested, we conclude that the Beneficiary was generally compliant with the Rules, as defined in the Objectives and Scope section above, for FY 2002. However, the results of our audit procedures disclosed two audit findings related to the Beneficiary not meeting the requirement to have an approved technology budget prior to filing an FCC Form 470 and missing and uninstalled E-Rate equipment items, which are reported below as Audit Finding Nos. 144339-F-2002-01 and -02, respectively.

In addition, the results of our audit procedures disclosed two beneficiary-specific other matters related to the Beneficiary not completing an FCC Form 500 in a timely manner and inadequate tracking of E-Rate equipment, which are reported below as Other Matter Nos. 144339-M-2002-01 and -02, respectively.

\* \* \* \* \*

### **Audit Findings**

#### ***Audit Finding No.***

**144339-F-2002-01**

#### ***Condition***

The Beneficiary's budget was not approved before submission of its FY 2002 FCC Form 470 in December 2001. The Beneficiary budgeted sufficiently, and obtained approval for its budget that addressed FY 2002; however, the budget was approved in June 2002, seven months after the submission of its FY 2002 FCC Form 470.

#### ***Criteria***

Per FCC Rule 54.504(b)(2)(v), applicable for FY 2002, at the time the Beneficiary submits the FCC Form 470, all of the necessary funding must have been budgeted and approved to pay for its non-discounted portion for the requested assets and services for the funding year.

#### ***Cause***

The budget cycle of the Beneficiary does not lend itself to the timing required by the Rules.

#### ***Effect***

There is no monetary effect due to this finding, since all non-discounted costs were paid by the Beneficiary to the service providers.

***Recommendation***

KPMG has no recommendation for the Beneficiary at this time and notes that the above referenced criterion is no longer included in the Rules.

***Beneficiary Response***

Because of the usually lengthy delay in the receipt of E-Rate funding approval versus filing of Form 470's in any given service year, the District has not in the past committed project moneys through the budget process at the time when any specific Form 470 has been filed. Rather, funds for projects in the application stage are not budgeted until the year in which it is most likely that the work or services described in any respective Form 470 will be done. To do otherwise would fly in the face of good budget-management practice, by forcing the District to "warehouse" funds for work or services that may or may not be approved to move forward. Given the high dollar values usually associated with E-Rate projects, this practice must continue in order for the District to remain fiscally sound.

***SLD Response***

In two places of the application process, the applicant is required to certify to certain information with respect to securing access to the resources necessary to use the services for which discounts are being sought. First, in Item 23 of the FCC Form 470 the applicant acknowledges that it is required to have "...all of the resources, including computers, training, software, internal connections, maintenance, and electrical capacity necessary to use the services purchased effectively. " The applicant also certifies "... that some of the aforementioned resources are not eligible for support." Second, in Item 25 of the FCC Form 471, the applicant certifies that it has "secured access, separately or through this program, to all of the resources, including computers, training, software, internal connections, maintenance, and electrical capacity, necessary to use the services purchased effectively....[It] certifies] that the Billed Entity will pay the non-discount portion of the cost of the goods and services to the service provider."



Funding Year 2002 program rules required that the applicant have the required resources when it filed its FCC Form 470. On August 13, 2004, the FCC changed the rules and modified this requirement in the Fifth Report and Order<sup>1</sup>. The new FCC rule 54.504(b)(2)(vi) states that “[s]upport under this support mechanism is conditional upon the school(s) and library(ies) securing access to all of the resources, including computers, training, software, maintenance, internal connections, and electrical connections necessary to use the services purchased effectively.” Schools and libraries, therefore, are no longer required to have secured access to the necessary resources at the time they file the FCC Form 470.

In the case of the Stockton Unified School District, the fact that it paid its non-discounted share indicates the District had the resources; therefore, no recovery is required. USAC concurs with this finding.

<sup>1</sup> See Fifth Report and Order at para. 66.

**Audit Finding No.**

**144339-F-2002-02**

**Condition**

During site visits, a total of nine switches funded for installation at Grunsky and McKinley Elementary Schools were not installed at their funded locations. Seven of these nine equipment items were not found during the site visits, one was found installed at King Elementary School, which was an E-Rate eligible school, and the other item was found uninstalled at the Beneficiary’s storage facility. The total cost of the seven missing switches and one uninstalled switch was \$18,117.

Subsequent to the audit, the Beneficiary conducted its own inventory review of all its E-Rate funded equipment for FY 2002, and disclosed that 9 switches and 1 UPS with a total cost of \$23,953 were missing, including the items identified by KPMG.

This is not a  
RULE - this is a  
reference to an  
ADMINISTRATIVE  
PROCEDURE

### *Criteria*

The monetary finding in the audit report is \$21,558.00 (post-discount) however, USAC's RIDF letter dated June 21, 2017 references a recovery amount of \$18,117.00. We cannot determine how USAC or KPMG arrived at this figure (whether it is PRE or POST discount) and though we have asked for documentation to support the amount, we have received nothing.

Perhaps more importantly, please note that this audit finding DOES NOT reference an FCC rule violation as there was no RULE in effect in 2002 that required an applicant to install or track inventory at the location listed on Form 471 nor was there a RULE in effect that required an applicant to keep detailed inventory records of E-Rate installed equipment. Those RULES were not codified until August 13, 2004 in the FCC's Fifth Report and Order.

In fact, USAC references this circumstance in their response to 144339-M-2002-02 on Page 22 of this Audit Report.

### *Summarized Beneficiary Response*

Per FCC Rule (54.507(d)), the deadline for implementation of non-recurring internal connections equipment is September 30 following the close of the funding year. In addition, USAC guidelines state that the Beneficiary should install all equipment at the site for which it was funded.

The Beneficiary indicated that there were several administrative errors made by both the Beneficiary and the service provider during the installation of E-Rate equipment that led to this finding. These included forecasting inaccuracies and insufficient tracking of installed equipment.

The monetary impact of this audit finding is \$21,558, representing the discounted cost of the missing/uninstalled equipment (computed as \$23,953 × 90% discount percentage).

The Information Technology Service group is responsible for distributing E-Rate equipment to the schools and should communicate to the school technology representative(s) the importance of tracking this equipment during and after initial installation. The Beneficiary should account for the missing equipment and ensure that E-Rate equipment is tracked appropriately going forward.

Because the Form 470 timeline required network specifications to be developed over one year before deployment, the designs by necessity included network additions and changes (such as portable classrooms) that were forecasted for the sites over the subsequent year. Upon receipt of E-Rate funding and deployment of the equipment by our selected service provider, AMS.NET, it was discovered that some of the forecasted network changes had been revised, thereby changing the equipment requirements at a few of the sites. The difference between forecasted network designs and actual network requirements found at deployment resulted in surplus equipment at the following sites: Grunsky Elementary, Elmwood Elementary, Montezuma Elementary, and Taylor

Though KPMG "summarized" the Beneficiary's Management response, there was a section that explained in detail that much of the equipment was found to have been deployed at DIFFERENT schools. This circumstance is not unusual in the course of deploying equipment purchased with support from the E-Rate program and is easily rectified through a service substitution or other post-commitment update however, in the early years of the program, these processes were not well defined. In fact, it was not until issuance of the FCC's Fifth R&O in August, 2004 that codification of this rule occurred and even then, there was a clarification issued on January 16, 2009 clarifying how and when USAC should seek recovery in scenarios that required clarification as they were not specifically addressed in the Fifth R&O.

### ***SLD Response***

USAC and KPMG are reliant upon a rule violation

ive Company (USAC)  
Y 2002  
15 BE 079

Stockton Unified School District  
Beneficiary No. 144339

Elementary. As other E-Rate schools were deployed, the surplus equipment was used to offset equipment deficiencies as they occurred at other E-Rate schools. Five E-Rate schools received some of the surplus equipment: August Elementary, Hazelton Elementary, ML King Elementary, Van Buren Elementary and Washington Elementary. All E-Rate schools listed were funded at the 90% level.

All equipment purchased with Schools and Libraries Program funds must be installed and be operational at the site referenced on the FCC Form 471. The applicant calculated their discount on Block 4, Item 10 of the Form 471 based on the site-specific or shared services they were applying for. Pursuant to 47 § 54.504 (b)(2)(v), the applicant certified on their FCC Form 470 and on Form 471, Block 6, Item 25, that they had sufficient funding to purchase all the resources necessary to make effective use of the eligible services requested in Block 5 of their Form 471. In FY2002, Commission Rule 47 §54.504(b)(2)(ii) required applicants to use the services purchased for educational purposes. Applicants violate these rules when they fail to ensure that they are effectively utilizing the services for educational purposes. USAC concurs with this finding, effect and recommendation.

### **Other Matters**

***Other Matter No.***

***144339-M-2002-01***

***Condition***

The Beneficiary had an excess of \$432,038 in total committed funds over total expended funds for FY 2002 that were not adjusted in a timely manner by utilizing FCC Form 500. Total committed funds for E-Rate FY 2002 were \$2,387,878 and total disbursed funds for the same funding year were \$1,955,840.



***Criteria***

Per the FCC Form 500 and related instructions, the Beneficiary should complete an FCC Form 500 to modify any FRN for which funds are not completely expended. By filing an FCC Form 500, the unexpended funds become available so that USAC can reallocate the funds as needed.

***Cause***

The Beneficiary was unaware of the need to file an FCC Form 500.

***Effect***

There is no monetary effect on the Beneficiary as a result of this matter; however, unused amounts for FY 2002 of \$432,038 could have potentially been utilized for other applicants.

***Recommendation***

The Beneficiary should file an FCC Form 500 when it determines committed funds will not be used during the funding year to release or cancel the FRNs so that the funds committed could be released and reallocated by USAC as needed.

***Beneficiary Response***

SUSD has been diligent in filing Form 500s to extend contract end dates and to cancel FRNs for projects for which we had decided not to move forward. The two FRNs mentioned were for recurring monthly service. During the E-Rate Year 5 funding cycle, we were not aware that a Form 500 was required to release unused funds from FRNs for recurring monthly services which were not entirely expended. It was our assumption that those funds would be released after the invoicing deadline had passed without a call being made for the monies.

The majority of the unexpended funds were for recurring service with SBC. Because of the difficulty we have had in determining whether we have received all of our E-Rate credits from SBC, we filed a request to extend the invoicing deadline with the SLD which was subsequently approved. Because of this, filing a Form 500 to reduce the amount of an FRN prematurely would jeopardize our ability to receive all of the credits that we are due from our service provider.



In the future, SUSD will file a Form 500 to release E-Rate funds from FRNs as soon as we can accurately determine the funding which is due to the District for that FRN.

***SLD Response***

There is no E-rate program rule requiring applicants to complete FCC Form 500 to report unexpended funds. Through outreach and training, USAC will continue to encourage applicants to complete and submit FCC Form 500 when committed funds are not needed. USAC concurs with this matter and recommendation.

***Other Matter No.***

***144339-M-2002-02***

***Condition***

During the audit, we noted inadequate control by the Beneficiary over the tracking, documentation, and delivery processes for E-Rate equipment. Of the nine schools chosen for detailed site visits, none had complete and accurate documentation corresponding to the delivery documentation maintained for that site. In addition, only five of the nine schools reviewed had complete and accurate inventory documentation to evidence the proper tracking and monitoring of E-Rate equipment.

***Criteria***

USAC guidance states that proper documentation should be maintained to evidence delivery, receipt, and monitoring of E-Rate equipment or services.

***Cause***

Based on discussions with the Beneficiary, this other matter was due to inadequate administration of the receipt, tracking, and installation of E-Rate equipment due to a compressed delivery and implementation schedule.

***Effect***

There is no monetary impact from this other matter.

***Recommendation***

The Information Technology Service group is responsible for distributing E-Rate equipment to the schools and should communicate to the school technology representative(s) the importance of tracking this equipment during and after initial installation. The Beneficiary should account for the missing equipment and ensure that E-Rate equipment is tracked appropriately going forward.

***Summarized  
Beneficiary Response***

Because E-Rate funding approval was not received on this project until February of the funding year, the timeline for completing the project was severely compressed. When funding was finally approved, the District was approaching the end of its multi-year contract for telecommunication services with its provider at that time, SBC. The need to complete the VOIP installation process in a window of slightly less than six months demanded a restructuring of the project's site-based rollout. This meant that installations were being performed at more than one site at a time, so equipment for multiple sites was received and stored in our District warehouse at the same time. When the equipment was ultimately deployed, the AMS.NET technicians performing the installation would take the model numbers and quantities from the warehouse as defined in our revised planning model, but apparently did not cross-check the serial numbers. In an ideal deployment, we would order, receive and install equipment for one site at a time; however, the timeline under which this work had to be completed in order to avoid costly telecommunication service duplication issues created an atmosphere that caused the contractor and the District not to work in this fashion.

### ***SLD Response***

Even USAC indicates in its response that for the Funding year being audited, there were no RULES associated with substantive, detailed record keeping or retention of those records. It was not until issuance of the FCC's Fifth Report and Order (August 13, 2004) that record keeping requirements were clarified and codified.

USAC's response to this matter is in conflict with their response to Finding # 144339-F-2002-02 as the audit finding and their response relies upon a 'rule violation' when such rule did not exist for FY 2002. Since there was no RULE in place in 2002 that required an applicant track E-Rate supported inventory, how could an applicant then be penalized for equipment that was not tracked?

In Funding Year 2002 it is an administrative function, not a program rule requirement to identify equipment and itemize it by make, model, and quantity. Going forward, the applicant should familiarize themselves with the FCC's Fifth Report and Order<sup>2</sup>, which clarified the record keeping requirements;" Schools and libraries shall maintain asset and inventory records of equipment purchased as components of supported internal connections services sufficient to verify the actual location of such equipment for a period of five years after purchase. For further guidance, the applicant should refer to the USAC website, "Schools and Libraries", "Reference Area" under "Demonstrating Compliance with Program Rules." USAC concurs with this matter and recommendation.

<sup>2</sup> See Fifth Report and Order at para. 47.

### **Improper Payments**

Based on the procedures performed and for the transactions tested for FY 2002, we noted improper payments of \$21,558 related to Audit Finding No. 144339-F-2002-02.



**APPENDIX 1: Selected FRNs, Related Reimbursement Forms, and Reimbursement Forms Selected for Testing**

				Reimbursement Forms for Selected FRNs		Reimbursement Forms Selected for Testing	
Selected FRNs	SPIN #	Service Provider	Form Type	#	\$\$\$	#	\$\$\$
800892	143002665	Pacific Bell	BEAR-472	0	0	0	0
			SPI-474	7	\$ 134,325	7	\$ 134,325
			Total	7	\$ 134,325	7	\$ 134,325
855948	143005880	AMS.NET	BEAR-472	0	0	0	0
			SPI-474	2	\$ 118,645	2	\$ 118,645
			Total	2	\$ 118,645	2	\$ 118,645
856036	143005580	AMS.NET	BEAR-472	1	\$ 111,587	1	\$ 111,587
			SPI-474	0	0	0	0
			Total	1	\$ 111,587	1	\$ 111,587
856935	143005580	AMS.NET	BEAR-472	0	0	0	0
			SPI-474	2	\$ 81,652	2	\$ 81,652
			Total	2	\$ 81,652	2	\$ 81,652
857235	143005580	AMS.NET	BEAR-472	1	\$ 78,026	1	\$ 78,026
			SPI-474	0	0	0	0
			Total	1	\$ 78,026	1	\$ 78,026
856498	143005580	AMS.NET	BEAR-472	0	0	0	0
			SPI-474	1	\$ 72,542	1	\$ 72,542
			Total	1	\$ 72,542	1	\$ 72,542
800917	143004610	Pacific Bell Internet	BEAR-472	1	\$ 25,993	1	\$ 25,993
			SPI-474	0	0	0	0
			Total	1	\$ 25,993	1	\$ 25,993
857724	143007617	Hewlett Packard	BEAR-472	0	0	0	0
			SPI-474	1	\$ 5,423	1	\$ 5,423
			Total	1	\$ 5,423	1	\$ 5,423
856804	143005580	AMS.NET	BEAR-472	0	0	0	0
			SPI-474	2	\$ 69,615	2	\$ 69,615
			Total	2	\$ 69,615	2	\$ 69,615
856634	143005580	AMS.NET	BEAR-472	0	0	0	0
			SPI-474	1	\$ 64,179	1	\$ 64,179
			Total	1	\$ 64,179	1	\$ 64,179
856728	143005580	AMS.NET	BEAR-472	0	0	0	0
			SPI-474	2	\$ 67,230	2	\$ 67,230
			Total	2	\$ 67,230	2	\$ 67,230
Totals				21	\$ 829,217	21	\$ 829,217

FRN 856760 (McKinley) is not listed on this Appendix though part of the 'amount' listed in Finding 144339-F-2002-02 includes some portion attributed to McKinley Elementary

## ***APPENDIX 2: Full Text of Beneficiary Responses***

### ***Audit Finding No. 144339-F-2002-02***

The RFPs which were developed and responded to in E-Rate Year 5 were based upon network designs that were created for each E-Rate school site early in the E-rate funding process. Because the Form 470 timeline required network specifications to be developed over one year before deployment, the designs by necessity included network additions and changes (such as portable classrooms) that were forecasted for the sites over the subsequent year.

Upon receipt of E-Rate funding and deployment of the equipment by our selected service provider, AMS.NET, it was discovered that some of the forecasted network changes had been revised, thereby changing the equipment requirements at a few of the sites. One site in particular, Grunsky Elementary, was significantly over-engineered at design, resulting in a substantial quantity of extra, unneeded equipment at the site. In recent discussions with the original design engineers, it has become known that the designs for Grunsky Elementary and ML King Elementary - a site which was significantly under-engineered - were inadvertently switched at the time of plan creation.

The difference between forecasted network designs and actual network requirements found at deployment resulted in surplus equipment at the following sites: Grunsky Elementary, Elmwood Elementary, Montezuma Elementary, and Taylor Elementary. As other E-Rate schools were deployed, the surplus equipment was used to offset equipment deficiencies as they occurred at other E-Rate schools. Five E-Rate schools received some of the surplus equipment: August Elementary, Hazelton Elementary, ML King Elementary, Van Buren Elementary and Washington Elementary. All E-Rate schools listed were funded at the 90% level.

We have attached a letter from the service provider used for this project, AMS.NET, which explains the methodology used in deploying this VoIP project. In an additional effort to fully quantify the equipment deployment, our Information Systems Department has now conducted a detailed inventory of each E-Rate Year 5 school site. We have attached their findings in a spreadsheet which shows all of the VoIP equipment located at these school sites, along with an accounting of any surplus equipment that was received and paid for by E-Rate funds. (*KPMG Note: The letter referred to by the Beneficiary is not included with this report.*)



***Other Matter No. 144339-M-2002-02***

We have attached a letter from the service provider used for this project, AMS.NET, which explains why the serial numbers on their packing slips do not always match the serial numbers of equipment they installed at a site. (*KPMG Note:* The letter referred to by the Beneficiary is not included with this report.)

Because E-Rate funding approval was not received on this project until February of the funding year, the timeline for completing the project was severely compressed. When funding was finally approved, the District was approaching the end of its multi-year contract for telecommunication services with its provider at that time, SBC. The need to complete the VoIP installation process in a window of slightly less than six months demanded a restructuring of the project's site-based rollout. This meant that installations were being performed at more than one site at a time, so equipment for multiple sites was received and stored in our District warehouse at the same time. When the equipment was ultimately deployed, the AMS.NET technicians performing the installation would take the model numbers and quantities from the warehouse as defined in our revised planning model, but apparently did not cross-check the serial numbers. In an ideal deployment, we would order, receive and install equipment for one site at a time; however, the timeline under which this work had to be completed in order to avoid costly telecommunication service duplication issues created an atmosphere that caused the contractor and the District not to work in this fashion.

As mentioned previously in this document, a detailed inventory of the District's E-Rate projects (all years) has been undertaken by District staff. All of the E-Rate Year 5 sites have already been completed. The attached spreadsheet provides that inventory, which includes serial numbers, district asset tag numbers, FRN information, deployment dates and payment information for each piece of equipment deployed. This inventory will be updated with any changes (due to warranty replacement, etc.) that may occur to the equipment at the site. The district will complete the inventory for E-Rate Year 6 and will track and document the delivery and deployment of equipment in subsequent E-Rate years using this same format.

The district has already taken steps to ensure that future E-Rate projects are tightly controlled and documented at the serial number level. Mostly these steps involve a stern reminder to our staff that they must adhere to the District's existing inventory control practices on all future E-Rate projects, regardless of their complexity.